

Hong Kong Exchanges and Clearing Limited and The Stock Exchange of Hong Kong Limited take no responsibility for the contents of this announcement, make no representation as to its accuracy or completeness and expressly disclaim any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this announcement.



Sinco Pharmaceuticals Holdings Limited

兴科蓉医药控股有限公司

(Incorporated under the laws of the Cayman Islands with limited liability)

(Stock Code: 6833)

KEY FINDINGS OF INTERNAL CONTROL REVIEW

Financial Adviser



Diligent Capital Limited

This announcement is made by the board (the “**Board**”) of directors (the “**Director(s)**”) of Sinco Pharmaceuticals Holdings Limited (the “**Company**” and, together with its subsidiaries, the “**Group**”) pursuant to Rule 13.09(2)(a) of the Rules Governing the Listing of Securities (the “**Listing Rules**”) on The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) and the inside information provisions under Part XIVA of the Securities and Futures Ordinance (Chapter 571 of the laws of Hong Kong).

References are made to the announcements (the “**Announcements**”) of the Company dated 26 September 2022, 30 September 2022, 24 October 2022, 8 December 2022, 13 December 2022, 4 January 2023, 21 March 2023, 27 April 2023, 18 May 2023 and 10 July 2023 in relation to the possible internal control irregularities, which probably involved unauthorised transactions during the six months ended 30 June 2022 (the “**Incident**”). Unless the context requires otherwise, the capitalised terms used in this announcement shall have the same meanings as those defined in the Announcements.

BACKGROUND

As disclosed in the Announcements, on 15 September 2022, the Company received the Letter from EY, being the then auditor of the Company, informing about the Incident which involved transactions that took place in January 2022 with a sum equivalent to US\$13 million (approximately HK\$100 million).

On 17 September 2022, the Board resolved to establish the Independent Committee to review and investigate the Incident, which comprised of four independent non-executive Directors, namely Mr. Lau Ying Kit, Mr. Wang Qing, Mr. Liu Wenfang and Mr. Bai Zhizhong.

On 20 September 2022, the Independent Committee appointed Diligent Capital Limited as its financial advisor and C&T Legal LLP as its legal advisor to assist in the investigation.

After conducting a preliminary assessment of the situation, the Independent Committee was of the view that the current information and evidence available to the Management was insufficient and therefore a proper investigation of the Incident with the assistance of an external forensic accountant was necessary.

Accordingly, on 21 December 2022, the Independent Committee appointed Grant Thornton Advisory Services Limited as an independent forensic accountant to conduct an independent forensic investigation into the Incident and produce a report on the findings of the Forensic Investigation to be presented to the Independent Committee.

On 15 March 2023, the Independent Committee received a draft Forensic Investigation Report from the Forensic Accountant.

On 21 April 2023 the Independent Committee engaged Moore Advisory Services Limited as the Internal Control Consultant to review the findings from the Forensic Investigation Report to ensure the Company has established adequate and effective controls to minimize the risk identified.

On 4 July 2023, the Independent Committee received from the Forensic Accountant the final Forensic Investigation Report.

On 27 September 2023, the Internal Control Consultant submitted the final internal control review report (the “**Internal Control Review Report**”) to the Independent Committee. Details of the report are provided below.

SCOPE OF THE INTERNAL CONTROL REVIEW

The scope of the internal control review under the Internal Control Review Report (the “**Internal Control Review**”) included the following for the period from 1 January 2022 to 31 March 2023:

1. management of procurement and payables process (goods and services);
2. management of treasury, investment and financing process; and
3. management of financial reporting and disclosure process.

KEY FINDINGS OF THE INTERNAL CONTROL REVIEW

The Internal Control Consultant identified 5 key internal control deficiencies in total, 3 of them were categorised as medium risk and the remaining 2 were categorised as low risk. As at the date of this announcement, the Company has already adopted rectification measures to address the key internal control deficiencies.

Set out below is a summary of (i) the internal control deficiencies that the Internal Control Consultant has identified; (ii) the implication of the internal control deficiencies identified; (iii) the recommendations for the rectification of the internal control deficiencies; (iv) the responses from the Company; and (v) the status of implementing remedial actions to address the internal control deficiencies as at the date of this announcement.

1. Management of procurement and payables

1.1 Date of contract signing (Risk level: low)

1.1.1 Findings and implication

When Sinco Sichuan agrees to a procurement order request, the merchandiser must apply for approval and seal on the contract through the office automation (OA) system. The supervisor of the import procurement department, Chief Legal Officer and Financial Controller of Sinco Sichuan, General Manager and Chairman of Sinco Sichuan will review the details of the order and the contract terms before the administrative department of Sinco Sichuan affixes the company seal to the contract. However, it was found in the sample tests that 24 out of 30 samples showed a contract approval date later than the signing date that was pre-filled on the draft contract. Sinco Sichuan did not update the pre-filled signing date before the actual signing of the contract, which made it difficult to determine precisely whether the transaction contract had been properly reviewed and approved by management before it was signed. Such practice may cause damage to the Group's interests.

1.1.2 Rectification recommendation

It is recommended that once Sinco Sichuan has drafted a sales and purchase contract, it should undergo the appropriate approval procedures before filling in the actual signing date of the contract so as to ensure that proper management approvals have been obtained before signing of the sales and purchase contract.

1.1.3 Response from the Company

The Group has agreed to follow appropriate contract approval procedures before signing of a sales and purchase contract.

1.1.4 Status of implementing remedial measures

The Internal Control Consultant considers that the recommendations have been implemented by the Company after reviewing the contract approval procedures of Sinco Sichuan.

1.2 Management of suppliers' information (Risk level: low)

1.2.1 Findings and implication

Pursuant to the guidelines of the Import Purchasing Management System (《進口採購管理制度》), the import procurement department of Sinco Sichuan should develop a comprehensive database of suppliers and keep it up-to-date through regular maintenance. Nevertheless, the authority list of the ERP system reveals that both the import procurement department and the finance department of Sinco Sichuan have the authority to modify and to create supplier records. Inappropriate delegation of authority could increase the risk of unauthorised access to the Sinco Sichuan's system.

1.2.2 Rectification recommendation

It is recommended that Sinco Sichuan's finance department's authority over the ERP system should be revised by removing its authority to edit and create supplier profiles.

1.2.3 Response from the Company

The Group has agreed to follow the recommendations and will no longer allow Sinco Sichuan's finance department to edit and create suppliers' profiles in the ERP system.

1.2.4 Status of implementing remedial measures

The Internal Control Consultant considers that the recommendations have been implemented after reviewing the authority of Sinco Sichuan's finance department over the ERP system.

1.3 Supplier background check (Risk level: medium)

1.3.1 Findings and implication

During the internal control review, it was noticed that Sinco Sichuan had made payments to third parties while establishing cooperative relationships or entering into distribution agreements with upstream suppliers. However, Sinco Sichuan did not conduct background checks on the third parties specified in the agreements to confirm their qualifications, business scope and affiliation with the upstream suppliers. This lack of proper background checks hinders the Group's understanding of the counterparties and third parties' actual situation, which can cause harm to the Group's interests.

1.3.2 Rectification recommendation

It is recommended that Sinco Sichuan should implement procedures of background checks on suppliers and retain the relevant information of the background check. When entering into cooperative agreements, Sinco Sichuan should confirm the background of the counterparties and third parties that are specified in the agreements, confirm their relationship with upstream suppliers, and maintain relevant documentation.

1.3.3 Response from the Company

The Group has agreed to follow the recommendations and has included supplier background checks in its procurement management system. Sinco Sichuan will confirm the background of all counterparties and third parties as stated in the agreements, verify their relationship with upstream suppliers, and maintain relevant documentation.

1.3.4 Status of implementing remedial measures

The Internal Control Consultant considers that the recommendations have been implemented after reviewing Sinco Sichuan's updated procedures for conducting background checks on suppliers.

2. Management of capital, investment and financing

2.1 Policies and Procedures (Risk level: medium)

2.1.1 Findings and implication

Every month, the Financial Controller of the Group prepares a monthly capital plan summary (《月度資金計劃匯總表》) recording the monthly expenses and the difference between such expenses and the budgeted amount. Then the Financial Controller reports and discusses these differences with the Company's management. However, the Group has not yet established formal written policies and procedures for these processes. This lack of comprehensive procedures for systems and policies may pose difficulties for its employees to comply with and for the organization to effectively administer those policies and procedures.

2.1.2 Rectification recommendation

It is recommended that the Group should improve systems for managing its capital, investment and financing to cover liquidity management issues, which includes cash flow forecasting. The relevant written policies should be reviewed and confirmed by the management before they are distributed to those responsible for relevant processes. Regular policy reviews are also required.

2.1.3 Response from the Company

The Group has agreed to follow the recommendations and will improve the systems for managing its capital, investment and financing so as to cover liquidity management issues such as cash flow forecasting. The Group's management will review and approve these policies before distributing to relevant process leaders. Also, the Group will regularly review and update these policies.

2.1.4 Status of implementing remedial measures

The Internal Control Consultant considers that the recommendations have been implemented after reviewing the Group's updated capital management system 《資金管理制度》 and budget management system 《預算管理制度》 for managing capital, investment and financing.

3. Management of financial reporting and disclosure

3.1 Policies and Procedures (Risk level: medium)

3.1.1 Findings and implication

The Group has specific procedures in place for financial forecasting, budget analysis, and foreign exchange and exchange rate management. Such procedures include:

- The finance department is responsible for preparing an annual budget summary, which will be signed by the financial officers of the Group, senior management of the Group and chairman of the Board for confirmation. Financial Controller of the Group will review the actual monthly expenses and report any discrepancies between the budgeted and actual amount to the management for discussion; and
- To effectively manage fluctuations in foreign currencies, Sinco Sichuan's finance department determines whether it is necessary to enter into any financial instruments by considering the volatility of the entire exchange rate market and the economic conditions. If deemed necessary, the finance department of Sinco Sichuan will fill out a bank application form for forward foreign exchange settlement and sale 《銀行遠期結售匯申請單》 and execute a currency forward contract with the bank. Approval from Sinco Sichuan's Financial Controller, General Manager and Chairman is required before executing the contract with the bank.

However, the Group has not established formal written policies and procedures for these processes, which leads to difficulties for the employees to follow and for the Group to administer the same.

3.1.2 Rectification recommendation

It is recommended that the Group should optimize its financial reporting and disclosure management system, which includes but is not limited to:

- financial forecasting and budget analysis; and
- foreign exchange and exchange rate management.

Policies and systems must be reviewed by management and signed off before distribution to relevant process leaders. Regular policy reviews are also necessary.

3.1.3 Response from the Company

The Group has agreed to follow the recommendations and is working on optimizing the systems and procedures for financial budgeting and analysis and foreign exchange management. This policy will be regularly reviewed to ensure its effectiveness.

3.1.4 Status of implementing remedial measures

The Internal Control Consultant considers that the recommendations have been implemented after reviewing the revised capital management system 《資金管理制度》 and budget management system 《預算管理制度》 which clearly sets out the responsibilities for financial forecasting and budget analysis, as well as the procedures for budget preparation and analysis.

VIEWS OF THE INDEPENDENT COMMITTEE AND THE BOARD

Having considered the Internal Control Review Report and the remedial actions taken by the Group, in particular, the Internal Control Consultant had performed follow-up reviews on the enhanced internal control measures adopted by the Group, the Independent Committee and the Board are of the view that (i) the above key internal control deficiencies have been remediated and the related risks have been managed to a reasonably acceptable level; and (ii) the remedial actions and improvement measures implemented by the Company are adequate and sufficient to address the key findings of the Internal Control Review Report.

By Order of the Board
Sinco Pharmaceuticals Holdings Limited
Huang Xiangbin
Chairman and Executive Director

Sichuan, the PRC, 27 September 2023

As at the date of this announcement, the executive Directors are Mr. Huang Xiangbin and Mr. Lei Shifeng; and the independent non-executive Directors are Mr. Lau Ying Kit, Mr. Wang Qing, Mr. Liu Wenfang and Mr. Bai Zhizhong.